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**TOURISM IN PERU: THE MISSING STRATEGY FOR  
ECONOMIC AND SOCIAL DEVELOPMENT**

by

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June 2006

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**TOURISM IN PERU: THE MISSING STRATEGY FOR ECONOMIC AND SOCIAL  
DEVELOPMENT**

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## **ABSTRACT**

In this thesis, the possibilities of tourism as a strategy for economic and social development in Peru are presented. Through the examination of previous governments, beginning with the Belaunde administration in 1963, the obstacles that Peru has faced in route to development are identified. Identification of the predominant issues at hand, unemployment, poverty and inequality, allows for further analysis of the policies implemented to stabilize the economy as well as provide immediate solutions for the above mentioned points of concern. It becomes clear that while the country is rich in resources, beyond natural resources such as crude oil and minerals, the promotion and enhancement of the tourism industry has rarely been used as a means of earning revenue. While there are a number of options to consider with regard to developmental strategies, the tourism industry presents definite opportunities for growth. These benefits are closely examined in this thesis, demonstrating how much Peru has to offer, not only to tourists who seek to broaden their cultural knowledge but most importantly to the Peruvian people, by way of a robust tourism sector.

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## I. PROBLEMS OF DEVELOPMENT

Sitting on a bus, packed with people leaving the city to return to their very modest homes which outlined one of the few major roads that would lead us to Pisco, I looked around me as if seeing things that I've known all my life for the very first time. Not two miles outside of Lima did things not only change, but they changed drastically. High rise buildings, upscale hotels, and very chic restaurants turned into small hut-like boxes, sporadic bodegas, and weathered faces that told stories of struggle, disappointment, neglect and most importantly the greatest desire to do whatever it takes to survive. So my question was, and still is, why such disparity between what seem to be two completely different worlds separated by only a few miles? Are these people content with their quality of life, despite knowing that change is not impossible?

Extreme levels of poverty and inequality are nothing new in Latin America, and particularly in Peru. They are unfortunate aspects of the historical heritage of the country's society that have remained relatively unchanged. The divisions created between dominant minorities of European descent and majorities of indigenous and mixed descent continue to exist, resulting in profound inequality in social participation as well as in income.<sup>1</sup> Rural majorities have for the most part been left out, disdained, or actively repressed by national leaders. This is demonstrated through the failure of the state to incorporate this sector of society in the process of

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<sup>1</sup> John Sheahan, *Searching for a Better Society: The Peruvian Economy from 1950* (Pennsylvania State University, 1999), 4.

development by denying them access to human capital-education, skills and economic mobility.<sup>2</sup> With this alone it is clear to see how development and economic transformation can be difficult to attain.

Economic and social transformations in a developing country can prove to be challenging, but not impossible, especially if the country has valuable natural resources. This is the case for Peru. Not only does the country hold a wealth of minerals, but it also possesses a plethora of beaches, jungles, and intriguing folklore. Unfortunately, amidst rampant corruption, devastating violence, and economic crises, the country has seemingly been unable to taper the infrastructural problems that the population has been suffering from let alone raise their heads high enough to look around them to notice that the answer to much their economic and social problems lay before them at arms reach, through the promotion and expansion of the country's tourism industry.

Focusing on tourism provides an avenue for Peru to address one of the key flaws in its current development strategy: generating mass employment. As this thesis will suggest, even when Peru has been able to sustain significant rates of economic growth, as occurred during the Fujimori and Toledo administration, this growth has not generated substantial increases in employment, further skewing the distribution of wealth in the country towards the rich. As a service sector industry, tourism is a relatively labor intensive industry compared to mining and manufacturing. It is also an industry in which Peru may have a strong comparative advantage due to the relative

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<sup>2</sup> Sheahan, 4.

abundance of natural beauty and rich history. In addition, it is likely to generate additional employment in those rural areas of the country where economic development has lagged. The purpose of this thesis is to demonstrate the need for the tourism industry to become a centerpiece of the economic strategy of Peru. This thesis first examines the traditional obstacles to successful development in Peru in Chapter I. Chapter II demonstrates that these problems have not gone unnoticed, analyzing the efforts that have been made, whether partially successful or utter failures, by numerous administrations, beginning with Belaunde in 1963. Chapter III will focus on the Fujimori administration. An entire chapter is dedicated to this particular regime as it demonstrates just how fruitful Peru can be if the appropriate measures are taken and policy implemented. With the initial success of the government in delivering a remedy to counter inflation, violence, and to a degree, unemployment, it would have seemed that the future was optimistic for Peru and its people. Unfortunately, just as it did in the administrations preceding Fujimori, self-interest took over what was of greatest importance, the best interest of the country, and the government took a very dramatic downfall. Finally, Chapter IV thoroughly explores the tourism industry; examining the positive and negative effects of an enhanced tourism sector; the regional inequalities of the tourism industry; and ultimately what has been done to promote the industry in an effort to build a sustainable source of revenue.

#### **A. INTRODUCTION**

The lack of both economic and social development in the country, outside of cities such as Lima, is a direct

reflection of governmental policy as well as its overall concern for the wellbeing of society. Between 1950 and present day, various reform policies have been implemented with promises of positive change that will in due course reduce both high levels of poverty and inequality. It is not that there have been no attempts to attack these problems, but rather it is the manner in which these attempts have been implemented and have sub sequentially taken form, that has hindered the ability for long lasting positive effects.

Through the analysis of individual governments and the economic policy orientation each took, beginning with Fernando Belaunde in 1963, there are various issues that stand out making the country's failure to develop understandable. Table 1 summarizes the main changes in government and policy orientation from 1963.<sup>3</sup> In conjunction with problems regarding policy implementation, is the inconsistency of policy regarding foreign investment and state intervention, both of which will be examined more closely below. Macroeconomic imbalance, abusive external borrowing which in turn leads to mounting deficit, a growing informal sector, and escalating violence add to the list of obstacles stagnating the development process in Peru.

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<sup>3</sup> Table 1 exerted from "Searching for a Better Society: The Peruvian Economy from 1950" by John Sheahan. Dates beginning from 1963 vice 1950 as depicted in the book for the purpose of covering those years examined in this thesis.

Table 1. Summary of changes in governments and economic policy orientation, 1963-1998

Year	Governments	Economic Policy Orientation
1963-1968	Democratic Election of promotional-reformist protection government (Belaunde)	Increased public investment and; political impasse over proposed land reform and foreign domination of the oil industry.
1968-1975	Radical reformist military (General Juan Velasco)	Greatly increased state intervention and protection; nationalizations and state firms; thorough land reform, rising fiscal deficit and heavy foreign borrowing.
1975-1980	Much more conservative military government (General Francisco Bermudez)	Partial reversal of Velasco reforms though continued extensive public ownership and high protection.
1980-1985	Democracy restored with Belaunde back, now more conservative and weakened by rise of <i>Sendero Luminoso</i>	Initial "neoliberal" changes; somewhat reduced protection but continued high public investment; excess spending and forced contraction.
1985-1990	All-out populism (Alan Garcia)	Intervention in all directions at once; heterodox program to promote expansion while blocking inflation by direct controls; intense conflict with private sector over attempted nationalization of financial system.
1990-2001	Neoliberal reforms combined with strand of authoritarianism (Alberto Fujimori)	Thorough reversal of state-led intervention; protection greatly reduced, and foreign investors welcomed back; extensive privatizations.

## B. INCONSISTENT POLICY FOR FOREIGN INVESTMENT

Foreign investment can take multiple forms and can affect development in a variety of manners depending on how the multinational firms investments are implemented into

policy. On one the one hand for example, there are those multinational firms who seek to cater to the higher income urban population. This firm is "rarely interested in exporting, and not primarily concerned with utilizing the country's own factors of production".<sup>4</sup> On the other hand, there are those who seek investment in order to take advantage of the low labor costs available to them as well as to earn foreign exchange. This second group is the one to take advantage of being that their search for cheap labor will aid in the reduction of unemployment and provide some sort of income to individuals who would otherwise have none. Unfortunately, Peru fell into the hands of the first all too eagerly and consequentially losing control of what should belong to the host country. "Foreign investment had become very important early in the twentieth century in mineral extraction, then gradually spread into domestic industry as well. An estimate of its extent is that firms under foreign control owned 46 percent of the fixed assets of all large manufacturing businesses by 1969."<sup>5</sup>

The fear of a takeover by these firms is understandable and is reflected in those policies implemented by governments that have chosen to close the doors to foreign investors completely, such as the Velasco government. While it is a very effective means of providing protection to state industries, it has more of a negative overall effect than positive. Shutting one door shuts many others, including one that leads to an increase in production capability and efficiency. Foreign investment

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<sup>4</sup> John Sheahan, *Patterns of Development in Latin America: Poverty, Repression, and Economic Strategy*. (Princeton, NJ: Princeton University Press, 1987), 164.

<sup>5</sup> John Sheahan, *Searching for a Better Society: The Peruvian Economy from 1950*. (Pennsylvania State University, 1999), 87.

allows for contact and competition with the outside world, which in turn creates the pressures necessary for technological progress and the improvement of productivity. With Peru, as well as much of Latin America, already seen as being inferior in terms of technological advancement, this form of contact is much needed.

Looking back at the policies implemented up to date, the constant back and forth efforts of Peruvian governments, in an attempt to find its way to development leave a strong possibility that investors will not want to invest in a country that cannot develop one consistent policy and make headway with it. The first extreme change in policy began with the Velasco government's strong turn against foreign investment. Expropriations were implemented, the state purchased foreign owned firms, and evident hostility toward foreign investors put the downward spiral in motion.<sup>6</sup> The first half of the 1980's looked promising for investors, but hostility quickly returned upon the election of Alan Garcia. With multinational firms essentially out of the picture and more than likely developing a questionable view of Peru as a country worth investing in, the Fujimori government re-opened the door to investment possibilities with open arms. The incumbent president reassured investors of their decision by bringing down inflation not to mention reassurance that the issues of security were under control with the capture of Abimael Guzman, mastermind of the guerrilla group *Sendero Luminoso*. Investment and industrial production rose strongly: from 1990 to 1997, value added by manufacturing increased 5.4

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<sup>6</sup> Sheahan, "Searching for a Better Society", 87.

percent a year.<sup>7</sup> While the end result was positive, there was never a long period of consistent policy regarding this issue.

In light of the progress made in the 1990's and despite the ultimate fall of Fujimori in 2000, it is evident that there are definite possibilities in making foreign investment successful for all parties involved. With the implementation of the right kinds of restraints and incentives there is hope for movement in the right direction.

### **C. MISDIRECTED STATE INTERVENTION**

The inconsistency of policy directed at foreign investment is a prime example of the misdirected character of the country's strategy of state-led development. The active measures taken through intervention were not the issue, but rather the form they took. "It made good sense to try to promote more modern and more dynamic industrial sectors, capable of innovation and continuing technical progress, but to shut out contact and competition with the outside world was a prescription going in the opposite direction."<sup>8</sup>

Looking beyond the benefits that can be derived through investment by multinational corporations, there are more basic matters that are requiring of the same, if not more, attention by the country's government and need to be addressed. First and foremost is the persistent failure of the state to provide equal access to education. Development *cannot* occur when a majority of the population is deprived of gaining the most basic skills needed to

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<sup>7</sup> Ibid, 87.

<sup>8</sup> Sheahan, "Searching for a Better Society", 188.



perform any job outside of the agricultural sector. As it is, there is insufficient arable land to accommodate the labor force, leaving migration as the only answer to possible employment. While urban jobs can be labor intensive and requiring minimal education, the negative aspect of technological advances shows itself in this regard. Increasingly, jobs outside of agriculture require skills acquired through higher levels of vocational education.

Second, is the issue concerning poverty levels and inequality, both of which result from the obvious lack of education and employment. While figures annotated in a wide range of literature concerning Peru show increasing numbers in each sector, the subject matter was not ignored entirely. Efforts made to resolve these major setbacks took the form of a variety of social programs that "have been closely associated with the adoption of more market-oriented economic strategies".<sup>9</sup> The programs developed intended to provide productive work rather than to provide traditional methods of support for the poor through measures that would interfere with the market by means of creation of subsidies or the increase of real wages.<sup>10</sup> In the long run, the social programs were short lived and cast aside when other issues considered to be of greater importance arose, as was the case of the Garcia administration. Two programs, the *Programa de Apoyo Directo* (PAD) and the *Programa de Apoyo de Ingreso Temporal* (PAIT) were initiated and quickly cast off upon indication that the government's mismanagement of the economy had lead

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<sup>9</sup> Sheahan, "Searching for a Better Society", 124.

<sup>10</sup> Ibid, 124.

to accelerating inflation. Not only were the programs abandoned, but also the Peruvian people who depended on it. Social spending decreased significantly and it hit an all time low of \$21 per capita, including education, public health, welfare and all other social programs during the initial years of the Fujimori administration.<sup>11</sup> It was not until the realization that elections were approaching in combination with pressures from international finance agencies that Fujimori stepped forward corruptly and intervened in an originally politically independent organization as a means of haggling votes from the rural poor.

Protection and the use of social programs as instruments of the state-led development strategy fell short in many ways. Protection essentially catered to the already high- income sector and social programs became a motivation of self-interest rather than genuine concern for the rural poor.

#### **D. MACROECONOMIC IMBALANCE & RISING EXTERNAL DEFICIT**

The second half of the 1970's was a period in which external credit was too plentiful for Peru's good, encouraging recourse to external borrowing to finance rising imports. As mentioned, Peru has been relatively slow in its technological progress and instead of using the resources that foreign investment could have contributed to enhancing that aspect, many governments turned to the foreign lending opportunities available to them to bring in the imported capital equipment needed. Of all the governments, the Velasco administration paved the way to serious macroeconomic imbalance and a rising external

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<sup>11</sup> Sheahan, "Searching for a Better Society", 125.

deficit that was a subsequent effect of the former. Imported equipment stimulated production by making it less labor intensive and more efficient however, that stimulation was not sufficient enough to bring production to the levels needed to earn adequate revenue from exports to pay off the debts incurred. With debt increasing on one end, the method used by the central government to cover its growing fiscal debt was to continue borrowing from other financial agencies abroad, creating an outrageous balance of payments deficit. The ease in which excess lending could be incurred was astounding, especially in Peru's case which proved to be very unique. With lending opportunities skyrocketing for a majority of Latin American countries despite their lack of ability to pay them off, the IMF developed what they thought would be a solution to the increasing balance of payments deficit. The plan required that a seal of approval by the IMF be acquired prior to any lending be agreed to by multilateral agencies. In 1977, during the Velasco administration, commercial banks agreed for the first time to refinance loans given to Peru without the seal of approval,<sup>12</sup> thus making this plan ineffective in tapering off the deficit situation. In the last three years of the Velasco government alone, the balance of payments deficit on current accounts rose from almost nothing to 10 percent GDP.<sup>13</sup> Such dependence on imports and the abuse of foreign lending to attain them reflects the inadequate attention placed on balances between spending and productive capacity.

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<sup>12</sup> Rosemary Thorp, *Progress, Poverty and Exclusion: An Economic History of Latin America in the 20<sup>th</sup> Century* (New York: Inter-American Bank, 1998), 214.

<sup>13</sup> Sheahan, "Searching for a Better Society", 138.

With governments that know no limits, how can development take a positive turn? Pressure to pay off debts takes focus away from the problems that need the most attention; the reduction of poverty and inequality.

#### **E. GROWING INFORMAL SECTOR**

The informal sector in Peru encompasses a large number of the population. Naturally, this is a result of the failure to provide adequate access to education and the excess of labor in comparison to the land available to the rural population as well as insufficient opportunities for productive employment. Table 2 demonstrates the sectors growing importance as a considerable amount of Lima's labor force is working in the informal sector.

Peru's informal sector does provide employment for many individuals, however this sector proves to be problematic in the sense that informals are not officially registered, giving them the opportunity to avoid any regulation, including taxes on their earnings. The only taxes paid are those placed on the products purchased from the formal sector. Evasion of taxes however is not their primary motivation; rather it is their means of survival in a country where their wellbeing is disregarded.

Table 2. Estimates of the percentages of workers in the informal sector and of domestic workers, Lima, 1970-

Year	Informal Workers as Percentages of the Labor force in Lima	Household Workers as Percentages of the labor force in Lima*
1970	31.6	9.8
1986	--	--
1990	40.7	5.1
1995	41.6	4.7
1996	--	4.2

\*Informal workers defined as self-employed excluding professionals, unpaid family workers and both owners and employees in firms with less than five employees. Domestic workers not included.

A study by Hernando de Soto in his book, *The Other Path*, presents the obstacles faced by migrants when they do in fact try to gain real authorization to initiate productive activities. He argues that the legal and institutional framework of the society included characteristics intended to protect existing privileges at the cost of development and entrepreneurship.<sup>15</sup> While the informal sector is in part a response by the poor to the obstacles placed in their path by the government and privileged class, it is an added problem for a society that needs revenue from taxation.<sup>16</sup>

During the later half of the 1980's for example, Peru experienced perhaps the most traumatic episode in their economic history under the administration of Alan Garcia Perez. The reformist program implemented was short lived, in particular the failed attempt to nationalize the

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<sup>14</sup> Table 2 excerpted from *Searching for a Better Society: The Peruvian Economy from 1950* by John Sheahan.

<sup>15</sup> Hernando De Soto, *The Other Path: The Invisible Revolution in the Third World* (New York: Harper, 1985), 100.

<sup>16</sup> John Sheahan, *Searching for a Better Society: The Peruvian Economy from 1950*. (Pennsylvania State University, 1999), 101.

country's banks. As a result of the administration's overall inability to "sustain a coherent policy coalition to support its reformist measures the formal economy declined and the informal economy expanded, depriving the state of crucial fiscal resources, particularly after the cutoff of international assistance by multilateral financial institutions in response to Garcia's unilateral decision to reduce debt payments to 10 percent of export earnings".<sup>17</sup> In the end, the fiscal crisis grew continuously; further weakening the government's already frail institutional, administrative, and coercive presence in society and adding fuel to the fire that guerilla violence in the more remote regions of the country thrived on.

#### **F. SOCIAL CONFLICT**

Violence in Peru was spurred by the country's history of failure to do anything about the extreme poverty of the rural areas, discrimination against the indigenous population, and the government's inability to generate adequate opportunity for productive employment. Sendero Luminoso, the most lethal guerrilla group that formed in the highlands of Peru, was able to gain tremendous support from the rural population for this reason. From the very beginning, attacks by Sendero were brushed aside as a problem for the highland region to deal with as though it were not a part of the country. Eventually, various districts were placed under states of emergency and the problem was delegated to the military. Human rights violations added yet another problem to the bag and became

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<sup>17</sup> Jo-Marie Burt, "State Making against Democracy: The case of Fujimori's Peru" in *Politics in the Andes: Identity, Conflict, Reform* (Pittsburgh, PA: University of Pittsburgh Press, 2004), 251.

a point of major concern, not for the government of Peru but rather for international human rights agencies such as Amnesty International and Human Rights Watch. Corruption and human rights abuses continued for the entirety of the Sendero Luminoso era, nearly 12 years, until the capture of Abimael Guzman in 1992. While Sendero's leader may be imprisoned, the group still remains and has continued to perform acts of terror to a lesser degree, making it evident that they have not disappeared completely. If the most basic issues of poverty and inequality continue to remain in the backburner, it will only be a matter of time until the violence of the 1980's reoccurs.

With so many issues to tackle, the most obvious problems need to be taken care of first. Through the examination of the different policy's implemented throughout the years, it is apparent that the problems identified in this section stem from important structural conditions which work against equality and the reduction of poverty: pressure of rapid growth of the population and the rural force running against the limits of scarce land, inadequate opportunities for productive employment outside agriculture, and highly unequal access to education, skills, and health care.<sup>18</sup> Once these issues are addressed and remedies are initiated, there is no doubt that progress can be made. While there are a number of options to consider with regard to developmental strategies, the tourism industry presents definite opportunities for growth. The benefits of a more robust tourism industry in Peru will be closely examined in a subsequent chapter, demonstrating how much Peru has to offer not only to the

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<sup>18</sup> Joe-Marie Burt, 149.

world through its fascinating history and beautiful culture, but even more importantly how much it has to offer to its own people through the use of its numerous resources. There is no doubt that progress can be made allowing Peru to achieve its potential for development. These resources are nothing new; they have always existed, simply never taken advantage of.



## II. ECONOMIC STRATEGY, 1963-1990

While Latin America is comprised of 20 independent countries, it is particularly interesting how each has undergone practically the same economic experiences. Some countries have encountered more difficulties generating development and employment. Adding to these already intricate difficulties, the entire region suffered from the temptation of foreign borrowing in the 1970's, causing for the debt that each country had already accumulated, to increase to considerable levels and ultimately leading to what we know as the Latin American debt crisis of the 1980's.

Peru has struggled to overcome similar obstacles in route to development. Its historical as well as current situation is comparable to several of its neighbors. The cities of Peru are beautiful and modern, however a short distance outside of the suburbs, lay miles and miles of shantytowns in which a significant majority of the Peruvian population live. Sights like these raise the question; how is it that the government could let such devastation persist, especially given that it is in fact the majority. What measures have been taken to alleviate this poverty-stricken country from the wrath of fiscal crisis, unemployment, poverty, and all that comes along with the territory of underdevelopment? Examining the administrations that have held the presidency beginning in 1963 with Fernando Belaunde Terry provides a base for examining why the conditions necessary for development fail to exist and from which the argument defining tourism

promotion as the missing strategy, for both social and economic development, is derived.

#### **A. IMPORT SUBSTITUTION INDUSTRIALIZATION**

Import Substitution Industrialization (ISI), has been a part of numerous attempts at stabilizing the Peruvian economy until the Fujimori administration put a stop to this unsuccessful strategy. For this reason it is important to first understand what it entails prior to delving into the analysis of the administrations of Peru.

The pursuit of Import Substitution Industrialization (ISI) throughout the region was stimulated by external shocks suffered in world trade caused by the Great Depression and World War II. While successful in some countries, specific characteristics of each influenced how far it proceeded and when it ran into crisis. ISI had a delayed beginning and limited progress in Peru, however when it was implemented it came in the form of rash policies during the 60's and 70's and helps explain the deep crisis it suffered in the 80's.<sup>19</sup> The reactions of first world banks to this crisis were uniform; they ended voluntary lending to most Latin American countries, which as we have noted earlier had become increasingly dependent on these loans. This in turn caused severe problems and instigated a domino type effect in regards to the economy. A huge financial drain that deepened fiscal crisis resulted from the drastic reductions in capital inflows and the strong pressures to maintain debt service. "Chronic fiscal deficits in turn fueled inflation, which hindered investment and growth, disorganized the economy, and

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<sup>19</sup> Kurt Weyland, *The Politics of Market Reform in Fragile Democracies: Argentina, Brazil, Peru, and Venezuela*. (Princeton & Oxford: Princeton University Press, 2002), 51.

unleashed distributional conflict."<sup>20</sup> Government plans at stabilization were unsuccessful and made things increasingly worse by interfering in the market. Hyperinflation was the ultimate effect in Peru with the combination of the deep fiscal crisis and the transition to unconsolidated democracy.<sup>21</sup> Hyperinflation is a very serious consequence to suffer, especially by a country whose population is largely poor and unable to take advantage of the type of financial mechanisms that middle and upper class Peruvians use to mitigate the impact of this condition. With this group of people bearing the most losses, support by the masses for bold stabilization measures increased.

There is a perception that political leaders and economic elites can foresee eventual fiscal problems, which may lead to crisis. This statement seems ironic being that if this were the case, it definitely overestimated the abilities of the first two governments to predict the outcome of their plans for economic development and stabilization, especially Belaunde. "If a chief executive faces the problems immediately and tries to prevent great losses before they come, strong popular support may not be received".<sup>22</sup> Essentially, when the most pain is being felt and when it seems that things couldn't possibly get worse economically, the more willing leaders and citizens are to incur risks and costs of systemic transformations.<sup>23</sup> This is an understandable statement, however was not necessarily

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<sup>20</sup> Weyland, 52.

<sup>21</sup> Ibid, 52.

<sup>22</sup> Ibid, 53.

<sup>23</sup> Ibid, 53.

the case in Peru as will be seen during in the following chapter during the regime of an outsider, Alberto Fujimori.

Returning to Import Substitution Industrialization measures pursued, there were inherent limitations posed by the limited size of markets and lack of competition that led inevitably to inefficiency. Early signs of economic problems prompted increasing efforts to complete national industrialization sustained by the increase in availability of foreign bank lending in the 1970's. Foreign banks pushed loans on Latin American governments, which ultimately through misuse lead to serious economic problems. Similar to an eighteen year old being issued a credit card for the first time, the easy access to international capital hindered the implementation of responsible adjustment plans.

#### **B. FERNANDO BELAUNDE TERRY, 1963-1968**

While it may be hard to imagine, there was a period when development took precedence over any other type of investment. This desire and focus of attention became characteristic of the early years of Fernando Belaunde Terry's first term in office, 1963- 1968. The phrase, "El Peru Construye" became a slogan associated with the government's economic philosophy during those years. The major manifestation of this attitude was a massive increase in public investment, massive increases in expenditure for construction, as well as large increases in social services particularly education and health.<sup>24</sup> The ultimate aim of the administration was to give the public sector a more active role in investment and social improvement, all

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<sup>24</sup> Pedro-Pablo Kuczynski, *Peruvian Democracy under Economic Stress: An Account of the Belaunde Administration, 1963-1968* (Princeton, New Jersey: Princeton University Press, 1977), 51.

objectives that following governments would promote in their election platforms without any success in implementation. "Belaunde displayed a healthy skepticism toward economist, and his love of Peru and its people often led him to digress from a financial discussion into a monologue on some new physical achievement of his government".<sup>25</sup> By all means, these were accomplishments deserving of attention, however what became most noticeable was the lack of direction regarding how to finance the development effort.<sup>26</sup> The Finance Ministry, the Development and Public Works Ministry, the Planning Office, as well as the Central Reserve Bank- all agencies principally responsible for economic policy- were not coherently combined nor was the talent available to really make each ministry of legitimate worth.

Equally important was the complacent views members of the government held regarding inflation. It was seen as an "inevitable concomitant to development"; unfortunately it was also an inevitable concomitant to fiscal and financial problems, which would only come into full view in the years following 1965.<sup>27</sup> Effective implementation of taxation was also an area that lacked structure during the Belaunde administration. The desired end state would have been an active and progressive tax policy, which in turn would have sought to strengthen and increase direct taxation on incomes and property. Instead,

The initial tax measures of the government reduced taxation of enterprises by widening exemptions on profits taxes and import duties to

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<sup>25</sup> Kuczynski, 51.

<sup>26</sup> Ibid, 75.

<sup>27</sup> Ibid, 77.

be paid by industry. At the same time, the level of import duties and of the turnover tax were raised. The strategy was to provide a stimulus to private investment, which had been lagging, while at the same time to raise revenue through taxes that were easy to collect. Initially, the measures led to a significant increase in revenue, but eventually the loopholes that had been opened became a major claim upon potential tax revenues. Moreover, the tax system came to rely even more than before on regressive forms of taxation.<sup>28</sup>

Fortunately, the means in which taxes were implemented were not drastically felt initially with the ability of domestic revenues to keep up with government revenues.<sup>29</sup> However, between 1963-1967, government revenues began to plateau. In the meantime, expenditures (teacher's salaries, growth of subsidies, military expenditures, and investment expenditures) continued to increase consistently and maintaining balance between the two became impossible. This was not a positive sign for the remainder of Belaunde's term in office, despite his initial intentions. The amount of funds available was grossly overestimated if taken into consideration at all.

Foreign loans and the use of domestic private savings became the primary means of dealing with the deficit. Neither of these methods proved to be effective enough to cover what was outstanding. Domestic inflation also continued to grow as the demand for imports increased, reaching an all time high by 1966. All signs were pointing to a future of serious economic and financial problems. Hopes were raised by the fortunate increase in demand for Peruvian exports at a time when international prices were

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<sup>28</sup> Kuczynski, 81.

<sup>29</sup> Ibid, 87.

escalating. Somehow "luck" reflected positively on the Belaunde government, seeming as though they had been able to cope with "a social situation more unbalanced than that of many other Latin American countries, and at the same time give new direction for the development of the country".<sup>30</sup>

Devaluation of the Peruvian currency, the *sol*, in 1967 became synonymous with the Belaunde period. Such an event becomes magnified politically after long periods of exchange stability and definitely takes a toll on the reputation of the government during which the devaluation occurred. "A modification of the exchange rate looks like a retreat for the government, and a personal defeat for the chief executive."<sup>31</sup> The demise of the exchange rate was rapid and drew much unwanted attention, especially from the military that would ultimately overthrow Belaunde from office.

The 1967 devaluation of the Peruvian sol by over forty per cent was one of a number of factors, which contributed to the ouster of President Fernando Belaunde Terry by the Peruvian military in October 1968. The military, having been critical of the Belaunde devaluation, appeared to have been committed to maintain the value of the sol, which was established in September 1967.<sup>32</sup>

### **C. GENERAL JUAN VELASCO ALVARADO, 1968-1975**

Of all the governments that have reigned over Peru, the period under Velasco is the most memorable for the lasting problems it left behind for successor administrations to try to resolve. Velasco began his term

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<sup>30</sup> Kuczynski, 103.

<sup>31</sup> Ibid, 151.

<sup>32</sup> Myron J. Frankman, *Foreign Exchange and Revolution: Peru, 1968-1973*. (McGill University, 1995)

in 1968 with an "emphasis on national autonomy, elimination of social control by the traditional landowner-export families, greater participation by workers in ownership and control of industry, and greater capacity for organization and self-help by the poor".<sup>33</sup> The desire to create a situation more favorable for the rural population is similar to those desires held by Velasco's predecessor. However, the outcome of his plan, predominately based upon land reform accompanied by high levels of protection for domestic industry and increased tax incentives for private industrial investment, did not take the path it had originally intended.<sup>34</sup>

Land reform was presented as a means to help rural workers by giving them ownership of the haciendas and commercially oriented plantations. Rural workers however compose a majority of the population of Peru, evidently making this a more difficult strategy to implement than expected. These difficulties became apparent when examining the large number of the rural poor left without any benefits of this new proposal that was supposedly aimed towards their development in society. Controversy was also instigated in the industrial sector upon the formation of a state program, "Industrial Communities". This program, similar to that of the land reform, aimed at bringing up the workers' share of ownership and thus giving them a voice in company management. The question that comes to mind however is, how can people who have a very limited education, successfully undertake a managerial role?

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<sup>33</sup> Sheahan, John. *Patters of Development in Latin America: Poverty, Repression, and Economic Strategy*. (Princeton, New Jersey: Princeton University Press, 1987), 237.

<sup>34</sup> Ibid, 258.



In conjunction with land reform, the Velasco government took away previous restraints on organization by introducing regulations that made it practically impossible for firms to discharge anyone who had worked longer than a brief trial period and by initiating regulations requiring profit sharing- intended to build up worker ownership.<sup>35</sup> This measure taken to protect the jobs of workers took a turn that the government did not foresee. Quality of work produced was compromised and aggravated employers decided that being forbidden to fire any long-term workers gave them the incentive not to hire at all.. Chaos and deterioration of the economy was the end state of this transformation and the result of macroeconomic mismanagement.<sup>36</sup>

Along with the steady demise of the agrarian reform and chaotic redistribution of managerial responsibilities, inflation began to escalate quickly. The Velasco government failed to respond appropriately, making choices to borrow abroad, keep interest rates down and foreign exchange cheap, impose domestic controls, and keep up the growth of spending.<sup>37</sup> There was also a feeling of hesitation when it came to multinational investment. These extreme measures of protection did more harm than good. First, it diminished contact with the outside world, which promoted healthy competition. Secondly, it denied the potential for technological advancements without depending on foreign lending to acquire the imports necessary to

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<sup>35</sup> John Sheahan. Searching for a Better Society: The Peruvian Economy from 1950 (The Pennsylvania State University, 1999), 136.

<sup>36</sup>John Sheahan. Patters of Development in Latin America: Poverty, Repression, and Economic Strategy. (Princeton, New Jersey: Princeton University Press, 1987), 237.

<sup>37</sup> Ibid, 261.

advance in that arena alone. Finally and most evidently, it caused for the administration to turn a blind eye to its increasing dependence on external borrowing, and external debt steadily rose.<sup>38</sup> Velasco's ideas of shared ownership and the regulations, which gave permanent job tenure to workers, were rejected whole-heartedly soon after he lost power. These reforms were discarded primarily as a result of the deterioration of the economy in combination with pressures from the IMF and most importantly the inability of the Velasco government to maintain a balance in his ideas of how a society should be managed and its willingness to take account of the preferences of the Peruvians people.<sup>39</sup>

**D. GENERAL FRANCISCO MORALES BERMUDEZ, 1975-1980**

General Francisco Morales Bermudez replaced Velasco in office in 1975 and remained in office until 1980. During this time his transitional military government was able to succeed moderately in resolving the issues of imbalance left behind by the former president. Bermudez started a necessary process of correction with relatively mild remedies, including fiscal and monetary restraint, rapid devaluation, and reduction of real wages.<sup>40</sup> All measures caused for the income of the rural population, particularly those who had already gained little from Velasco's reforms, to decrease by nearly 13 to 15% during this five-year period alone. The measures taken were far from ideal, the poor took the brunt of the effort to fix the overall balance and the plan of devaluation began to accelerate

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<sup>38</sup> Sheahan, "Patterns of Development", 261.

<sup>39</sup> Ibid, 263.

<sup>40</sup> Ibid, 266.

making the rate of inflation grow increasingly worse.<sup>41</sup> The unfortunate factor in all this was that because of the rash reforms, which were implemented in the previous regime, these measures were imperative despite the negative form they took. Devaluation was of particular importance. This was a mild shock the population had to deal with in order to get the economy back in order, however, as usual, when the appropriate time came to cut down on the rates of devaluation and exercise caution on monetary expansion to stagnate the rate of inflation, proper measures were not taken to do so. Instead, the rate of growth of the money supply was allowed to rise, overshooting the rate of inflation.<sup>42</sup> Consequently, inflation rose progressively as a result of not taking the appropriate measures at the appropriate time.

#### **E BELAUNDE'S SECOND TERM, 1980-1985**

Belaunde made a comeback at a time when the Shining Path was going public for the first time and Peru's informal sector had grown to a level that surpassed any legal business sector. To add to these problems, he also was faced with other pressing problems, to include "establishing future relations with the armed forces, reigniting economic growth, dealing with the demands of a mobilized popular sector, and recognizing and devising a strategy to confront the Shining Path".<sup>43</sup>

In terms of economic policy, Belaunde had high hopes for restructuring the country's dying economy and sought to cure unemployment through the creation of over 1 million

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<sup>41</sup> Sheahan, "Patterns of Development", 266.

<sup>42</sup> Ibid, 266.

<sup>43</sup> Peter Flindell Klarén, *Peru: Society and Nationhoods in the Andes* (New York: Oxford University Press, 2000), 373.

new jobs. Contrary to what he had originally intended for Peru, his plans took a completely different direction upon his appointment of Manuel Ulloa as prime minister. Formerly Belaunde's Minister of Economy, Ulloa remained a firm believer of neo-liberalism and devised a policy prescription designed to, "enhance the market by reducing the economic preponderance of the state, removing tariff protection from industry, and encouraging private foreign investment".<sup>44</sup> For a short amount of time, the strategy had its glory with renewed confidence in the country by foreign investors and banks as demonstrated by the influx of loan opportunities and privatization. By 1982 however, public support for Belaunde's liberalization plan decreased with the realization that its promises of increased GDP and employment were not being delivered. In addition to these delivery failures, inflation began to accelerate and loans were being held back as the signs of deterioration began to surface.

With economic conditions worsening, the low-income groups in the highland regions were suffering the most. The administrations liberalization policies were causing further deterioration of living standards of a majority of Peruvians while feeding into the hands of a select privileged few. Belaunde and his team did recognize this negative turn of events, however his "efforts to address these disparities and the deepening distress of the poor were inadequate".<sup>45</sup> He continued to pursue measures that made cuts in social programs, further aggravating the population and subsequently causing for social unrest to

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<sup>44</sup> Klarén, 374.

<sup>45</sup> Ibid., 376.

increase and feed into and strengthen the influence of the Shining Path.

As seen in Belaunde's previous term in office, while his plans for stabilization were well intended, they fail drastically upon implementation. With inflation having increased considerably, the already existing gap between state and society continually widening, and a renewed accumulation of debt, Belaunde exited his political career with little to show but a great deal of economic turmoil for future administrations to handle.

**F. ALAN GARCIA, 1985-1990**

The turn to heterodox experiments taken in the 1980's by Alan Garcia were inspired by the failures of orthodox measures taken by the previous administrations. Having faith in the promises of heterodox experts regarding the feasibility of cost free stabilization and theories of inertial inflation, Garcia "embraced the claim that renewed development would lower inflation by eliminating economic bottlenecks".<sup>46</sup> Plan Inti was developed, having the political advantage of promising to bring about economic stability in a distributionally neutral and politically cost free fashion.<sup>47</sup> A temporary price freeze was recommended by heterodox experts, as was the plan to create a new currency and peg it to the dollar. This plan aimed at breaking the inflationary mentality by linking the currency to a stable foreign currency.

The views of Garcia's economic advisors emphasized the requirement for increases in production and investment in order to achieve stabilization and the need to implement

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<sup>46</sup> Weyland, 72.

<sup>47</sup> Ibid, 81.

tax and interest rate cuts.<sup>48</sup> They also sought to reduce the fiscal drain on the state by limiting external debt service by 10 percent of export revenues in order to leave the government with ample resources for stimulating domestic development.<sup>49</sup>

Initial heterodox measures proved to be successful, however were short lived. With difficulties growing, Garcia took a bold move and sought to nationalize the private banking system. This step was "designed to force higher investment and stem capital flight and thus counteract the increasing hesitancy of the private sector, which had come to regard the heterodox program as unsustainable and therefore refused to invest at the levels sought by the government".<sup>50</sup> There was strong opposition to this move and eventually Garcia had to put his plan in the backburner. Distrust increased substantially among the business district and to make matters worse the economic crisis became even more severe than before. As usual, the bold move that failed in the end hurt the poor sectors of the country, which means the majority of the population.

In light of the persistent deterioration of the economy, Garcia was forced to look at more orthodox measures in the hope of salvaging what he could of the economy and his reputation. He adopted five rather orthodox stabilization packages, which still retained heterodox elements, such as price freeze.<sup>51</sup> His efforts failed to lower inflation but succeeded in producing severe recession and deepening the poverty level, if that was at

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<sup>48</sup> Weyland, 84.

<sup>49</sup> Ibid, 84.

<sup>50</sup> Ibid, 86.

<sup>51</sup> Ibid, 89.

all imaginable. Failure plagued his stabilization plans once again and he switched back to more heterodox policies in hopes of bettering the situation as quickly as possible, which in turn would aid in redeeming himself in time for the 1989 elections. Failure occurred again unsurprisingly and he ultimately attempted to adopt tougher orthodox stabilization measures. His inability to come up with a decisive plan and even worse, settle on one method of stabilization developed a severe aversion to not only himself but also toward the professional political class that he essentially represented.

#### **G. CONCLUSION**

While each of the governments examined in this chapter did have intentions of targeting the major issues of poverty and inequality through their economic strategies, no significant changes were accomplished except for the return to democracy in 1980 following nearly ten years of military rule. There was however initial success in nearly all reforms implemented. However, as was typical of the cycle of Peruvian strategy implementation, initial success in economic strategy ultimately deteriorates to failure due to the lack of focus on the major issues at hand: poverty and inequality. Although these plans often raised expectations among Peruvians for a better quality of life, the economic development that resulted rarely generated a sufficient amount of employment necessary to significantly reduce poverty, particularly in the rural areas. This contributed to violence across rural Peru and a constant cycle of political crisis at the national level.

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### III. FUJIMORI: GROWTH WITOUT EMPLOYMENT

At the time of the 1990 presidential elections, conditions in Peru were at the brink of complete disaster. While the economic decline had been the result of years of crisis, the Garcia administration's experiment with heterodox economic policy contributed significantly to the continuous erosion of the country both socially and economically. Economically, less than 10 percent of the population was adequately employed, real wages had decreased drastically, the average household consumption fell 46%, income distribution became increasingly skewed, and GDP had fallen by 25 percent between the years 1988 and 1990 alone.<sup>52</sup> Socially, poverty levels increased sharply throughout the country, spending on public health and education fell 30%, and the country's overall infrastructure fell into a state of severe disrepair as the leading guerilla insurgent group, Sendero Luminoso, continued to gain strength and make its way into Lima.

After years of crisis and growing disillusionment with the political class, the Peruvian people were more than ready for change. Peru's economy would take a drastic turn towards a truly draconian orthodox stabilization package, following the disastrous era of the Garcia administration. Initially presented by presidential candidate Mario Vargas Llosa, this program called for a harsh IMF-like stabilization program that would ultimately re-integrate the county into the international market after years of isolation during the Garcia administration. Vargas Llosa's "shock" program would include measures to: liberalize

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<sup>52</sup> Klarén, 406.

trade, resume full debt payments, encourage foreign investment, privatize state enterprises, eliminate price controls and subsidies, overhaul the tax structure, and construct a free market economy that would replace the failed statism and mercantilism of the past.<sup>53</sup>

Unwilling to accept the harsh terms of the program, the population responded negatively to this proposed solution to the country's problems, subsequently taking their votes, which had originally supported Vargas Llosa in the first round of the presidential elections, and casting them in favor of Alberto Fujimori. Fujimori campaigned strategically, promising a moderate and less painful solution to the economic disarray and targeting the needs of the rural inhabitants, which comprised a majority of the population and consequentially a majority of the votes. He pledged to make governmental credit easily accessible to informals and campesinos and also to provide legal protection to street vendors, both big promises that benefited an ever-growing sector of society. His descent also became one of his greatest advantages as the struggles that had been overcome by the Japanese immigrants in Peru, classified him as other than the typical political class, justifying his motto of being "*un presidente como tu*". Ultimately, while rival Mario Vargas Llosa had won the first electoral round by 3 points, Fujimori pulled ahead significantly in the second, defeating his opponent with 62% of the vote.

This chapter examines the policies implemented during this administration, the effect the policies had on the economy as well as the population, and ultimately what led

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<sup>53</sup> Klarén, 403.

to the fall of what could have been the most promising regime to take the reigns of the country.

#### **A. THE EARLY YEARS**

Upon taking office on 28 July 1990, it became apparent to the newly elected president that he had inherited a disaster and the moderate strategy to economic recovery upon which he won the presidency would not work in these circumstances. Ironically, by 1991, Fujimori implemented a much harsher stabilization program than that which had been designed by Vargas Llosa and subsequently rejected by a majority of the population. The orthodox stabilization package consisted of a series of measures aimed at attacking runaway inflation and reconstructing the Peruvian economy through: state privatization, deregulation of financial and labor markets, tax and tariff reform, investment incentives, decentralization of some social services, and the reduction of social spending<sup>54</sup>.

The design of the stabilization program that was implemented were harsher than what would have been desired by the population, as it mimicked what they had voted against, thus leading to "further pauperization of the population". Real income decreased by one-third, overall consumption declined 24 percent, the total population of Peruvians living in poverty increased to a high of 54 percent, and finally the proportion of under or unemployed increased with levels of inequality rising accordingly.<sup>55</sup> These early consequences were expected however, and promises of a social emergency program were made to lessen the toll it would take on the poorest segments of the population. Expenditures made on the social emergency

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<sup>54</sup> Klarén, 407.

<sup>55</sup> Ibid, 408.

programs were nowhere near the \$400 million originally allotted, but rather only \$90 million was actually spent. Disregard for the poor changed gradually from 1993 on however, with an increase in social programs from 2 percent GDP for the first year of Fujimori's government to 6 percent by 1995.<sup>56</sup> Support remained high for this seemingly radical president, despite the severity of the preliminary phase of shock treatment. "Peruvians yearning for political authority and economic stability was so great that they would accept whatever actions the new president took to resolve crisis."<sup>57</sup>

Fujimori's first year to eighteen months in office did achieve some relief for the country. Repercussions of the harsh measures taken allowed for payment of foreign debt that had amounted to \$21 billion by 1990. Through the development of SUNAT (the National Tax Administration), which made strenuous effort to raise tax collections, and by holding down government spending, the government gave priority to resuming service on external debt.<sup>58</sup> Immediate implementation of regular payments of \$60 million to International Financial Institutions renewed confidence in Peru, finally pushing the country into the right direction and reintegrating it into the world economy.

As confidence in Peru was renewed, public investment in the country rose accordingly. Originally held down through 1991, it increased to 25 percent by 1994, partly stimulated by aid from international development agencies as a result of the further downturn of the economy in early 1992. The investments made by multinational corporations

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<sup>56</sup> Sheahan, "Searching for a Better Society", 158.

<sup>57</sup> Klarén, 408.

<sup>58</sup> Sheahan, "Searching for a Better Society", 157.

assisted considerably in the reconstruction of Peru's public infrastructure, which had not only been battered by the violence of Sendero Luminoso but also suffered from the basic disregard for its maintenance.

The long-term issue of runaway inflation also began to diminish. The reduction of protection was intended to reduce inflation by "allowing buyers to switch to imports whenever domestic prices of particular goods rose above external levels and by increasing the flexibility of the production process through more open access to imported supplies".<sup>59</sup> By 1992, only two years into his presidency, inflation dropped to 55 percent from a crushing 7650 percent.

High public opinion, concurrence from opposition party FREDEMO regarding this stabilization package and his neo-liberal economic goals in conjunction with the policy making powers derived from the Constitution of 1979, concentrating power in the chief executive, fostered the increasing arrogance and authoritarian tendency that was beginning to surface towards the end of 1991. Having little representation in Congress, a pact with the Peruvian armed forces was established and the military became Fujimori's main institutional foundation of the new regime.<sup>60</sup> With this, Fujimori chose as principal advisor of military affairs, Vladimiro Montesions, who was already stained with a discharge from the army for allegedly passing information to the United States and specializing in defending drug traffickers. Existing tensions between the executive and Congress intensified upon Fujimori's apparent abuse of decree powers as he took the liberty to

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<sup>59</sup> Sheahan, "Searching for a Better Society", 158.

<sup>60</sup> Klarén, 409.

exploit the graces given by the presidential honeymoon period. By November, 120 decrees had been issued, aiming at liberalizing the economy and reconstructing the state. On April 5<sup>th</sup> of the following year, Fujimori took one drastic step further, carrying out an *autogolpe* (self-coup). This entailed the suspension of the Peruvian Constitution, the closure of Congress, and the eventual dismemberment of the Judiciary. Fujimori announced the creation of a "Government of Emergency and National Reconstruction" that would prepare the way for "true democracy".<sup>61</sup> While the end goal was supposedly democracy, this did not fare well with the international community. Economic aid and support was withdrawn almost immediately, jeopardizing Fujimori's entire economic recovery plan of reintegrating Peru into the world economy. Due to international pressure, elections for a constituent assembly to rewrite the constitution were held in May, with municipal elections to be held later that year. Regardless of having to give into these pressures, Fujimori managed to tailor it all to meet his ultimate desires.

#### **B. AUTOGOLPE OF 1992**

The autogolpe implemented in 1992 implanted the virus of corruption that plagued the Fujimori administration and led to its eventual demise. As previously mentioned, the international community was not in agreement with this new plan and ultimately the Organization of American States (OAS) forced the Peruvian government to restore "democratic institutionality" via the application of a newly constructed constitution to be followed by municipal

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<sup>61</sup> Klarén, 413.

elections.<sup>62</sup> Soon after, the Democratic Constituent Congress (CCD) was formed, of which 44 of the 80 seats went to Fujimori's Cambio 90 affiliates, with the purpose of drafting this new constitution.

In October of 1993, the new Constitution was proposed, highlighting one notable change, which permitted the reelection of the president to a second consecutive term, thus opening the door for Fujimori in the upcoming 1995 elections. In addition to this change, it tightened laws on terrorism, consolidated institutional power at the top, and created a more centralized state, all modifications which gave the chief Executive ultimate power. With an already weak system of checks and balances, the autogolpe evidently further eradicated any remaining obstacles, namely the legislature and the judiciary, which may have prevented Fujimori from remaining in power for a second consecutive term. Ultimately, this was his main objective as we see the transition of holding office become a selfish economic benefit than an overall political one. This same transition was visible not only in the role of the president, but also in all parties that took part in the politics of the Fujimori government.

Upon the ratification of the new Constitution, the tables turned in regards to which sectors of society supported the government and the changes that were being implemented. Support for the President, among lower income groups decreased due to the government's failure to generate growth or real income, despite the drastic reduction in hyperinflation.<sup>63</sup> In order to regain the

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<sup>62</sup> Catherine M. Conaghan, *The Immoral Economy of Fujimorismo in The Fujimori Legacy: The Rise of Electoral Authoritarianism in Peru* (Pennsylvania: The Pennsylvania University Press, 2006), 109.

<sup>63</sup> Klarén, 418.

backbone of his support, social spending aimed at alleviating the distress imposed upon the urban and rural people, as a result of the "Fujishock", needed to be increased in a hurry. Acknowledging where his efforts needed to focus, Fujimori developed a program to sell off state owned enterprises. This program initially received negative responses from the private sector, especially when considering the odds that foreign firms would want to invest in a country characterized by a "terror-infested, low exchange rate, high interest rate, and volatile" history that Peru had suffered.<sup>64</sup> Contrary to popular belief however, this program in conjunction with the newly reformed tax program- that streamlined the two main tax institutions (SUNAT and SUNAD), slashed the numbers of taxes, and raised both individual and property taxes- lead to the dramatic rise in much needed revenue. Central Bank reserves climbed from a deficit of \$143 million to over \$6 billion by the end of 1994.<sup>65</sup> With these accomplishments in his pocket, Fujimori sought to expand his control to eventually micromanage all of the government's social programs and in due course assume monopoly over public works as well. Attaining these goals was a given in his case, having gained a significant amount of public support through his ability to deliver the above mentioned demands, crush runaway inflation and for the most part, defeat Sendero Luminoso through the capture of leader Abimael Guzman in September of 1992.

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<sup>64</sup> Klarén, 418.

<sup>65</sup> Ibid, 420.



### C. BEHIND THE SCENES

The ability to deliver promises, or at least more promises than previous administrations had even attempted to deliver, masked the insurmountable corruption that circulated behind the scenes of the Fujimori administration. Corruption was the primary constitutive feature of the regime, the "cartilage and collagen that held it together and ensured its reproduction".<sup>66</sup>

Greed rings were rampant, and while the overall intent by all involved was to maintain Fujimori in power, even beyond the second term that he had attained through reconstruction of the Constitution, individual rings generated for personal benefit. Fujimori's security advisor, Vladimiro Montesinos, arranged illicit deals with numerous high-ranking public officials, brokers, and top commanders in the Peruvian Armed Forces. These transactions ranged from deals with narcotraffickers to deals with legislative officials to abandon their political organizations and side with Fujimori. The later became the primary means of securing an unheard of third term for the President.

On top of Montesinos' dealings and those of civilian policy makers to include officials from the Ministry of the Economy, Fujimori himself had developed a greed ring of his own that involved the transfer of gross amounts of money to Japan. With his sister and brother-in-law serving as Peru's ambassadors to Japan, these transactions flowed in and out of the country with little speculation. The above-mentioned family members also managed the creation of two non-profit foundations, Apenkai and Aken, which aimed at raising money in Japan for philanthropic projects in Peru.

<sup>66</sup> Conaghan, 103.

"An estimated \$42 million flowed through a complicated maze of domestic and foreign banks set up by the president's relatives to manage the foundations' finances".<sup>67</sup> This estimate, supposedly coming directly from personal accounts, raises tremendous speculation as it surpasses the modest salary of the president. Questions regarding Fujimori's excess spending and ability to produce unusual amounts of money at a moments notice were brought to rest when the presidents' former wife, Susana Higuchi, reported that she had found a sum of \$110,000 in a safe in the private quarters of the palace.<sup>68</sup> Considering the supposed modest pay of the Peruvian president, this amount is well over the personal budget of the president.

With evidence of corruption continually surfacing, support for Fujimori dwindled. With the 2000 elections approaching, this was a less than favorable situation to be in if the administration was to succeed in maintaining office and continuing with their lavish lives, financed by corruption. When April 9<sup>th</sup> (preliminary elections) arrived, Fujimori lost the absolute majority. This loss spurred an even greater corruption scandal masterminded by Montesinos, *Operation Recruitment* came into play. Monthly pay offs of \$15-20,000 were made to Congress members who fell into the trap of Montesinos, contingent that they either desert their political organizations and side with Fujimori or agree to act as spies, informing Montesinos of activities of the opposition in Congress.<sup>69</sup> This, as all of the illicit transactions made, became a very costly means of campaigning from which public sources were robbed. The

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<sup>67</sup> Conaghan, 108.

<sup>68</sup> Ibid, 108.

<sup>69</sup> Ibid, 111.

Ministry of Defense, Ministry of Interior, the Armed Forces and SIN (Peru's National Intelligence Service) funds were the primary donors, although unknowingly.

#### **D. CONCLUSION**

For the first time in decades, Peru had managed to creep out of its hole of economic crisis and head in the right direction for development, at least initially. The Fujimori administration delivered promises of social development, an escape from runaway inflation, debt payments, and the reintegration into the world economy. It seemed too good to be true, and in the end it was. The truth is, that the developments that had managed to actualize during this administration are a taste of what "could be".

Besides pointing out the degree of corruption that took place during Fujimori's terms in office, the examination of this particular administration offers constructive insight to what measures have proven to be of value in the developmental process. The administrations recognition of the importance of foreign investment is particularly notable, especially when considering how important of a role investment plays in the development of a strong tourism industry. Just as Fujimori used the revenue brought in through the investment of multinational firms to rebuild a worn down public infrastructure, the same methodology can implemented today to continue with the strengthening of the state infrastructure and to sharpen the once grim image of Peru. The beautification and modernization efforts will draw in further investment, primarily in the service industry; hotels, resorts, restaurants, etc.

Additionally, taking into account the amount that had been embezzled in the corruption that kept Fujimori and his cronies in power, it is evident that the opportunity for development was riper than ever. While efforts were made to target the problems that had caused Peru to land in the situation it had been in for years, namely poverty and inequality, it is a fair to say that the wealth that filled the pockets of the Fujimorista's failed miserably to trickle down. Some schools were developed, roads built, and health care centers constructed, however it is crucial to highlight that while significant developments they are, it is not enough to bring the country and its population of from the depths of despair. The number of these projects could have been double what they were and the quality of service provided could have been more than *just* adequate. Roads could have been built, public works could have been further developed to provide basic resources to those who needed, and continue to need them most.

An unfathomable amount of money was essentially wasted during the Fujimori administration. While the question of "what could have been" will always remain when reflecting on this particular administration, the Fujimori experience should serve as a lesson learned, demonstrating the vast possibilities that exist for development and hopefully leading individuals in office to direct investments into more tangible projects that could generate significant employment, such as tourism.

#### IV. TOURISM EXAMINED

The underlying cause of Peru's problems is the poverty, inequality in social services and employment issues that plague each region of the country. Chapters II and III demonstrate that while these problems have not gone unnoticed by numerous administrations, they have essentially remained unchanged despite various efforts to lessen their devastating impacts. Each president since Belaunde's first term in 1963 has sought to increase public investment, expenditures for construction, as well as large increases in social services primarily in education and health.<sup>70</sup> Unfortunately, while the initial motives were good, the implementation of these policies fell severely short of achieving the desired outcome. Other economic crises, which were a direct implication of the issues noted above, became more of a priority and took over political and economic decisions. Corruption, as seen predominately during Fujimori's regime, also deprived the country from countless possibilities of development. Taking into account the billions of dollars embezzled by the administration, so much more could have been accomplished in terms of the country's infrastructural development.

On the flip side of the similarities shared by the various administrations, we also see many differences when comparing the economic policies of Belaunde, Velasco, Garcia and ultimately Fujimori. Peru has had an eclectic history when it comes to policy implementation, adopting strategy's ranging from an extreme reform in the

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<sup>70</sup> Pedro-Pablo Kuczynski, *Peruvian Democracy under Economic Stress: An Account of the Belaunde Administration, 1963-1968* (Princeton, New Jersey: Princeton University Press, 1977), 51.

distribution of land to the most draconian style stabilization program. Given the abundance of natural beauty and culture that Peru has been blessed with, nowhere has the value of tourism been taken into significant consideration and incorporated into economic strategy. Given that income inequality and lack of employment are fundamental shortcomings of Peru's current development strategy, the aggressive development of the tourist industry may provide a remedy by creating a labor intensive service industry in a sector in which Peru has a comparative advantage.

Presently, the current president, Alejandro Toledo, in conjunction with his officials in the Ministerio de Comercio Exterior y Turismo (MINCETUR) has developed an actual plan of action, the Plan Estrategico Nacional de Turismo (PENTUR), in an effort to bolster the tourism sector of Peru. While this is a step in the right direction, the plan identifies its primary objectives yet remains vague in defining concretely how these objectives will be accomplished. This chapter's focus is to examine how Peru can benefit from a more robust tourism sector by first identifying the benefits and detriments of the industry, analyzing the regional inequalities in the tourism sector, and finally by examining what efforts have been made towards the improvement and promotion of this overlooked asset.

#### **A. BENEFITS OF THE TOURISM INDUSTRY**

Peru has enormous potential for tourism development with the vast number of attractions that that can accommodate all interests, ranging from culture to urban tourism. With this, it is important to note the value of

the industry and the linkages it has with sustainable development. These are economic, social and environmental linkages, which have further ties that affect and are affected by other sectors such as transport, health, and cultural heritage sectors.<sup>71</sup> Figure 1, excerpted from a recent study supported by the World Bank, presents the impacts (positive and negative) that the various sectors within the identified linkages have as a result of tourism.

There are three major areas where incoming tourism makes a positive addition to a country's economy:

1. Contributions to GDP
2. Encouragement of inward investment
3. Increase in opportunity for employment<sup>72</sup>

Through an increase in foreign exchange earnings from hotels, restaurants and other tourism related groups, it is evident that a robust tourism industry can contribute to the country's overall GDP. While Peru possesses the means for increasing GDP, the lack of current available domestic capital, as a result of years of poor economic policy implementation, makes the development of a stable tourism infrastructure increasingly difficult. Foreign investment however, is an important instrument through which development can occur. Chapter III analyses the Fujimori regime, and in doing so calls attention to the possibilities presented to the country by way of foreign

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<sup>71</sup> Taylor, Pedroso and Anil Markandya, "Tourism and Sustainable Development: Lessons from Recent World Bank Experience," in Proceedings of Tourism and Sustainable Economic Development Macro and Micro Economic Issues jointly organized by CRENoS (Università di Cagliari e Sassari, Italy) and Fondazione Eni Enrico Mattei, Italy, and supported by the World Bank (Chia Laguna Hotel, Sardinia, Italy, 19-20 September 2003), 2.

<sup>72</sup> Les Lumsdon and Jonathan Swift, *Tourism in Latin America* (New York: Continuum, 2001), 31.

investment. In regard to this particular sector of the economy, the potential for development is excellent. Studies have shown that in light of other development issues, Peru, similar to a majority of Latin American countries, has suffered from a funding gap in the tourism sector and governments have been reluctant to invest in substantial tourism projects.<sup>73</sup> Consequently, because the government overlooks the benefits of investment beyond the privatization of Peruvian corporations the tourism sector has been relatively starved of the investment necessary to stimulate growth that would be of equal benefit to numerous sectors of society.

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<sup>73</sup> Lumsdon and Swift, 34.



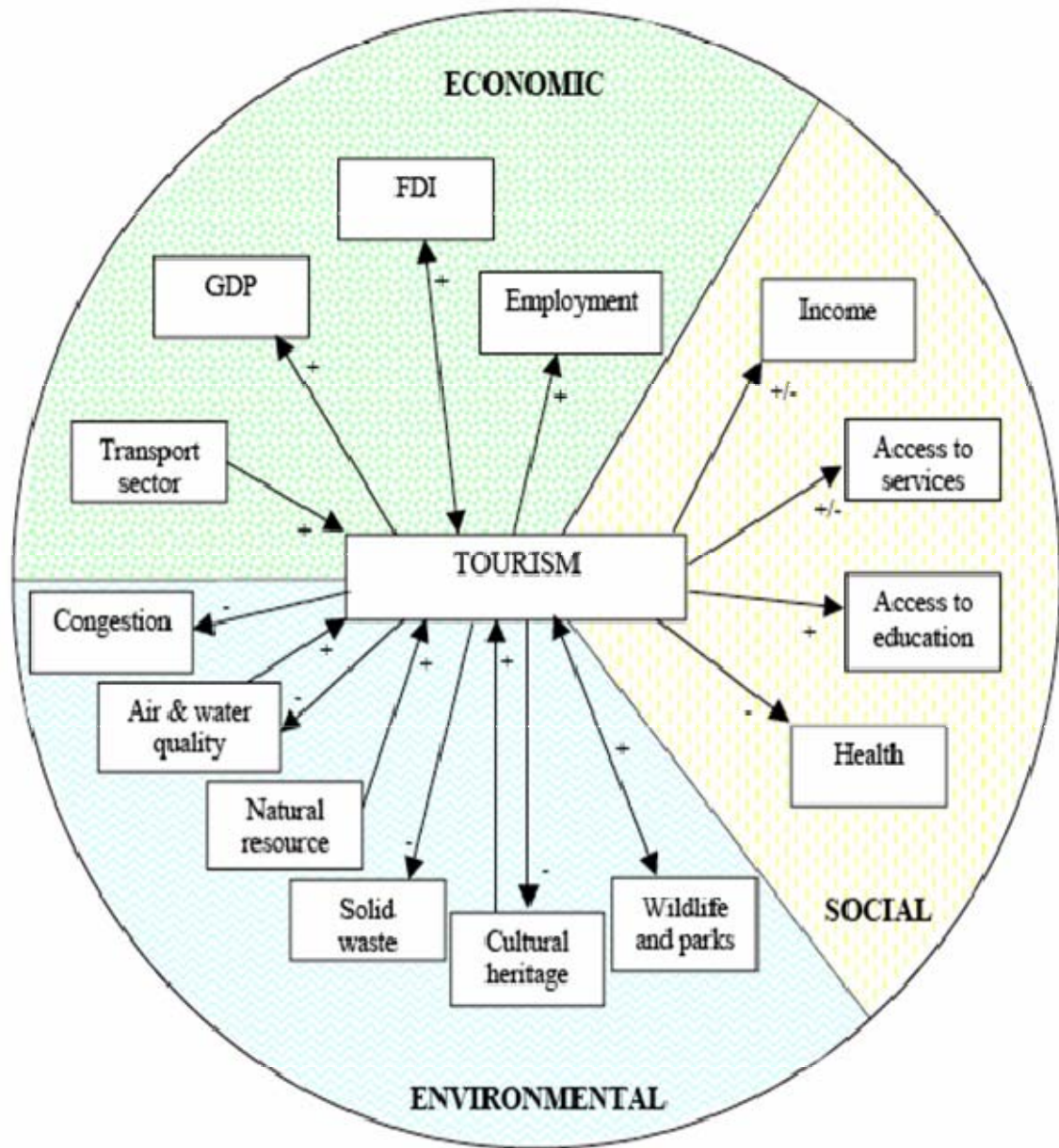


Figure 1 Linkage between World Bank Projects and Sustainable Development

On the social level, investments made into the hotel and restaurant sectors of the industry cater to the needs and demands of tourists, which in turn prove to be favorable to a much broader majority of the population vice

benefiting the slim number of individuals comprising the political and industrial elite. For example, electricity, water, sewage, etc. are all common and basic services that most tourists, especially those traveling from developed countries, enjoy in their homeland. Services such as these however have unfortunately been denied to a large majority of the Sierra and Selva regions of Peru. With this deficiency, the only means of attracting travelers and sustaining their business is to provide these services. By default, the population normally deprived of water, electricity, sewage and such would benefit from these improvements, proving that the advantages of tourism extend beyond the economic and reach far into the social development of the otherwise severely underprivileged rural majority.

Socially and economically, the tourism industry opens the doors for employment. These opportunities provided in the services sector cannot go unnoticed, especially considering the wide range of underemployment and unemployment that persists throughout Peru. While there are arguments that rebut the impressive opportunities presented for employment through this sector, and will be examined below, the catalyst to job openings is that this industry, contrary to the traditional manufacturing industry, is exceptionally labor intensive. The average number of employees per hotel room, for example, is estimated at two, depending on the type of hotel and the local skill base.<sup>74</sup> Notably, hotel type jobs are considered to be good as they have good working conditions, comparatively speaking, and relatively good pay.<sup>75</sup> While

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<sup>74</sup> Taylor, Pedroso and Markandya, 6.

<sup>75</sup> Ibid., 6.

the level of education of most of the rural population is limited, the skill level required to fulfill a janitorial staff for example is not terribly demanding. For positions requiring greater proficiency skills, there is a government-sponsored institution, El Centro de Formacion en Turismo (CENFOTUR), which provides training in specialized areas. Programs include but are not limited to bartending, culinary education, business management, sales, cultural entertainment and customer service in travel agencies and airlines. Currently, CENFOTUR is located in Barranco, a section within Lima; however with the appropriate allocation of funding it would be more than possible and advantageous to develop extension schools into other cities outside of the capital. By doing this, an increased level of education becomes available to the population, which in turn broadens employment openings and opportunities. Also worthy of mention is the role women play in this sector, with the percentage of females working in this sector higher than that in other economic sectors.<sup>76</sup>

Scholars pessimistic towards the development of this industry find most contention in the impacts tourism *could* have on the environment. There are definite possibilities that an influx of tourism in one location could be erosive to the environment, however the efforts put into preserving the environment often go unnoticed. La Reserva Nacional de Paracas (National Reserve of Paracas) for example, is one project that demonstrates these efforts. Created in 1975, the National Reserve of Paracas is one of Peru's most protected areas of the country. Its primary objectives including:

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<sup>76</sup> Taylor, Pedroso and Markandya, 9.

- The conservation of the marine life ecosystem with concentration on fish, birds, and marine mammals
- To grant special protection to endangered species
- The preservation of Peru's cultural and historical heritage
- To develop techniques of rational use of some "hidrobiologicas" species
- To develop facilities for recreational, educational and cultural use
- To contribute to the economic development of the region<sup>77</sup>

The Nasca lines are also found in this same site, making Paracas an attraction rich location. Accommodations however are severely lacking, with only one hotel with continuous running water. With the appropriate funding to enhance the exterior image of the region, tourism here could flourish, providing substantial revenue for the population, for the upkeep of the reserve and protection of the environment.

In addition to The National Reserve of Paracas, the World Bank's Global Environmental Facility has supported and funded projects linked to tourism that aim at protecting the country's environment. The Participatory Management of Protected Areas Project-Peru specifically seeks to:

- (a) Ensure biodiversity conservation by strengthening the capacity and involvement of the communities and the private sector to sustainably manage the protected areas and (b) to obtain sustainability for the financing of recurrent costs. A subcomponent of participatory protected

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<sup>77</sup> El Mundo Azul, a nongovernmental organization that provides information regarding the preservation of the environment. Website supported by Peru.com  
[http://www.peru.com/mundoazul/la\\_costa/paracas.asp](http://www.peru.com/mundoazul/la_costa/paracas.asp)

area management is the development of sustainable economic activities, one of which is wildlife management for tourism development and use of tourism services (e.g., research, educational awareness).<sup>78</sup>

Evidently, the environmental effects of tourism have not gone unnoticed, but have rather been focused on as a means of drawing in revenue for the preservation of its regions and wildlife. Again, with the appropriate funding directed towards the enhancement of the tourism industry these efforts can be enhanced significantly, causing development to be inevitable.

#### **B. NEGATIVE IMPACTS OF THE TOURISM INDUSTRY**

Despite the benefits noted above, there are impacts that may take a negative turn. Some literature suggests that tourism does little to bridge the gap between developed and developing countries, stating:

There is no clear link between tourism growth and economic development, owing to many other complicating factors such as inflation, the ability of an area to diversify and the willingness of the local population to work hard.<sup>79</sup>

While this statement seems far-fetched, it does hold some truth; if the industry is not closely monitored and policy is not tailored to thwart the problems that may arise, countering the economic and social benefits that have been previously addressed. Surprisingly, while one of tourism's greatest contributions is to the country's economy it is also one of the industry's most debated issues along with

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<sup>78</sup> Taylor, Pedroso and Markandya, 19.

<sup>79</sup> Holloway, J.C. The Business of Tourism (London: Pitman Publishing, 1988), 252.

the impacts the sector may have on the socio-cultural environment and the natural environment.

With the value of tourism lying predominately on economic factors and emphasizing the positive contribution of tourism to the economy,<sup>80</sup> the negative impacts can occasionally go unnoticed. The creation of local or regional imbalances within the economy, exacerbating the already existing inequality of income distribution between rural and urban zones, leads the list of counter arguments.<sup>81</sup> The subject of inflation also arises when examining tourism, and while it is difficult to make a direct correlation between the industry and inflation, it has been done. This argument asserts that:

The nature of International Tourism implies an increasingly greater degree of world wide economic integration. In addition to the increased wage levels and pressures on real estate in cities, tourism can be said to have contributed to inflation and a negative balance-of-payments level through the importation of (expensive) foreign goods.<sup>82</sup>

Foreign investment as well as the overall concept of foreign travelers visiting and imposing their demands on the population has become an additional target of negativity in conjunction with the above mentioned economic impacts. Foreign investment presents a double-edged sword. While this sort of investment is exceedingly important for developing countries, multinational corporations introduce their technologically advanced versions of the already existing smaller industries such as airlines, travel agencies, hotels, restaurants, etc. Being that most

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<sup>80</sup> Lumsdon and Swift, 191.

<sup>81</sup> Ibid., 191.

<sup>82</sup> Ibid., 192.

developing countries, and Peru in particular, have continuously sought to gain stature in the technological field, this should be seen in a positive light. Contrarily however, scholars have come to view this more as a threat to resident industries thus overwhelming local interests.<sup>83</sup>

On a socio-cultural level, the threat comes in the form of personal interaction. Essentially it opens the eyes of the population, particularly the rural population, to the possibilities of development. Necessities that visitors demand will be expected to be delivered, despite the fact that the country being visited often times does not have the means to provide particular services as they may not be part of or considered to be part of their "cultural standards". In the end, it has been stated that:

When mass tourism from highly industrialized societies is introduced into an economically underdeveloped country, the contrast between the two societies is apt to be stark and the consequences often great ... The difference between the consumer habits of the tourists and the living conditions of the indigenous population is thus accentuated and the differences between the two societies emphasized.<sup>84</sup>

Along the same socio-cultural lines, traditions such as arts and crafts and ceremonies observed by the population become threatened by commercialization. By contrast, yet equally negative, some communities may be forced to stray from modernization for the sake of maintaining the interest of travelers. Tourists often expect to see Indigenous communities unaffected by time and

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<sup>83</sup> Lumsdon and Swift, 193.

<sup>84</sup> Ibid., 195. Quote in Lumsdon and Swifts *Tourism in Latin America*, referencing Lothar Nettekoven's 'Mechanisms of Intercultural Interaction' in *Tourism: Passport to Development? Perspectives on the Social and Cultural Effects of Tourism on Developing Countries* by Emanuel de Kadt (New York: Oxford University Press, 1984)

living in an extreme version of "traditional village life". While it is important to maintain a cultural identity, the "issue is to what extent the 'traditional' Indian community remains a developmental time warp in order to seek economic gain by whetting the appetites of the tourist markets".<sup>85</sup>

In addition, the effects tourism may have on the environment take a central role in countering the benefits of the industry. The list that has been derived linking tourism to environmental damage is extensive, including:

1. Congestion
2. Increased pollution loads in both water and air
3. Use of resources, particularly fresh water and energy resources
4. Solid waste generation
5. Degradation of cultural heritage
6. Ecological Impacts
7. Impacts of induced settlement

To emphasize the above-mentioned points, the case of Machu Picchu has been expounded upon as it is the predominant cultural site visited in Peru. However, it is important to note that this location has suffered damage primarily due to poor management and while the argument is valid and attempts to point out the negative side of tourism, it actually plays into the hands of just the opposite position. Promoting the numerous other cultural, nature based, and urban tourism sites that exist in Peru would alleviate Machu Picchu and a selective handful of other locations that have been promoted by the government of such issues as congestion, waste generation, and increased levels of pollution.

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<sup>85</sup> Lumsdon and Swift, 199.



### **C. REGIONAL INEQUALITIES: PROMOTION AND TOURISM INCOME DISTRIBUTION**

To date, the negative effects of tourism have often outweighed the positive effects in Peru due to the regional inequalities that are discussed in this section. "With a rich cultural and archeological heritage, scenic landscapes, varied climates, diverse natural ecosystems and beaches, the quality of Peru's tourism attractions are outstanding".<sup>86</sup> Despite the vast diversity of attractions, Machu Picchu is Peru's primary site that has become the defining attraction of the country's tourism industry in conjunction with Lima, the capital city. With high levels of concentration in these two areas, the negative impacts of the industry are effortlessly proven. However, as previously mentioned, a more evenly distributed tourism sector would significantly benefit the country in the development process all the while easing those negative effects that could disintegrate the value of specific regions of the country.

Analyses show that the tourism sector brings tremendous benefits to the region in terms of GDP and employment creation, particularly through the revenue brought in through the hotel and restaurant sectors.<sup>87</sup> More detailed analyses however, further demonstrate the inequalities that exist within the industry. Inequalities rest primarily in that the revenue brought in from the industry promotes the development of the already better-off departments versus the poorer ones.<sup>88</sup>

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<sup>86</sup> Greg O'Hare and Hazel Barrett, Regional Inequalities in the Peruvian Tourist Industry in *The Geographic Journal*, Vol. 165, No. 1. (Mar., 1999), 53.

<sup>87</sup> Ibid., 47.

<sup>88</sup> Ibid., 47.

In an effort to analyze the regional inequalities in the tourist industry, it is important to first look at how the country is divided. Peru consists of three physical regions which are broken up as follows<sup>89</sup>:

1. Western Departments (10):
  - a. 46% of the population
  - b. 10 Departments
  - c. Generates 80.5% of the country's GDP
  - d. Consists of Lima-Callao metropolis included in this region which forms the economic heartland of the country with 54% of the nation's GNP
2. The Sierra (Highland Region):
  - a. 50% of the population
  - b. 9 Departments
  - c. Mostly Indigenous Amerindians
  - d. Poorest part of the country with only 12.5% of the country's GNP
3. The Selva:
  - a. 4% of the population
  - b. 5 Departments of the Amazonas
  - c. Generates 7% of the nation's annual wealth from the sale of timber and petroleum.

A study completed in 1997 by Mendoza Quintana, examined these divisions and the consequent regional inequalities of the industry through the calculation of each region's Tourism Attractiveness Index (TAI). Five resource categories are employed in the evaluation of the TAI, to include:

1. Natural Sites
2. Cultural, historical and archaeological heritage
3. Folklore
4. Technical, scientific and artistic works
5. Tourist programs and events

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<sup>89</sup> Information regarding the regions division exerted partially from the Background section of O'Hare and Barrett's article, Regional Inequalities in the Peruvian Tourist Industry, 48.

Without going into great detail as to how calculations are obtained, the method used by Quinta has proven to be a useful tool in providing an overall impression of the distribution of the country's tourism resources.<sup>90</sup> The final evaluation of the study demonstrates just how uneven the tourism industry in Peru truly is, revealing that many resource rich areas do not receive the tourism that would be expected given the resources available in accordance with the calculated Tourism Attractiveness Index (TAI), making them resource rich/tourist poor departments.<sup>91</sup> A prime example of such a department is that of Ancash, which has an TAI of 73.74 (Table in Figure 2, col. 9) and drawing a number of tourists- represented in col. 1 of the Table in Figure 2 through the mean annual number of bed nights stayed by foreign travelers- comparable to other departments which have a significantly lower TAI index (Tacna). While the figure representing the number of bed nights stayed is by no means meager, the gaping disparity between bed nights in respect to specific departmental TAI is astounding. Figure 3 further exemplifies this point of widening disparity, graphically demonstrating the "departmental distribution of the mean annual (1985-96) number of foreign tourist bed nights in relation to the Departmental Tourist Attractiveness Index of Mendoza Quintana's 1997 study".<sup>92</sup>

After examining the TAI's provided through Quintana's study, it is notable that very few departments in Peru have a Tourism Attractiveness Index below ten. These numbers

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<sup>90</sup> A detailed description of how the Tourism Attractiveness Index (TAI) is calculated can be found in O'Hare and Barrett's article, *Regional Inequalities in the Peruvian Tourist Industry*, 53.

<sup>91</sup> Ibid., 54.

<sup>92</sup> Ibid., 52.

beg the question, why are only a select few departments, primarily the Cuzco and Lima/Callao departments, the most widely traveled by *foreign* tourists? It is important to be aware of the distinction between the type of tourists, domestic and foreign, when answering this question as it demonstrates the promotional weakness of the tourist industry.

The tourism industry has suffered primarily at the hands of the government, chiefly in their failure to provide a stable infrastructure that would support an industry that accentuates the country's attributes. Without the appropriate transport systems, adequate lodging, and a vigorous promotion strategy such an industry will not survive at the levels necessary to advance developmentally. In regards to transportation, Peru's outlying regions are inadequately served in comparison to the more developed cities: roads outside stretching into the Selva or more remote regions of the Sierra are few and far between; the railway system is small; services are generally poor and journeys slow, subject to constant stoppages and derailment; and air transport facilities outside of Lima, which is a necessity for most tourists where distances are great, roads are poor and terrain difficult, are of poor quality and not equipped for night flights thus leading to congestion of flight times.<sup>93</sup> Such deficiencies hamper the potential of the county in promoting its numerous attractions and enhancing the industry as a whole. More over, without a means of reaching a particular destination there is hardly any point in promoting it.

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<sup>93</sup> O'Hare and Barrett, 54.

Tourist services are also an area in which the industry is severely lacking. This shortcoming seems unexplainable considering that El Centro de Formacion de Turismo (CENFOTUR) was developed in 1940 in an effort to "improve the quality, efficiency and productivity of Peru's tourism workers and prepare them to assume management and supervisory positions in the hospitality industry".<sup>94</sup> In 1995 alone, enrolment was at 1,791 students, 30 percent higher than it had been the previous year.<sup>95</sup> With such a large number of people having received training to hold positions in the industry, the quality of service should be exquisite and ample. It is the poor distribution of quality hotels and restaurants throughout the country that stagnates employment possibilities and restrains the industry from flourishing, not necessarily the lack of individuals possessing the skill base necessary for employment. A recent study examining the regional pattern of tourist services points out that Lima alone holds 46.3% of the country's total tourist accommodations with 31% of the hotels and 30% of the restaurants.<sup>96</sup> Cuzco on the other had, despite the average 287 thousand foreign tourists that come to explore the vast Inca Empire, only possesses 7.3% of the total accommodations.<sup>97</sup> Looking beyond basic accommodations, quality hotels and restaurants (Four and Five Stars) are highly concentrated in the capital. O'Hare and Barrett note that in 1996, "there were thirty

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<sup>94</sup> Matt A. Casado, "Peru's Tourism Industry: Growth, Setback, Threats," Cornell Hotel and Restaurant Administration Quarterly (February 1, 1998), 6.

<sup>95</sup> Ibid., 6.

<sup>96</sup> O'Hare and Barrett, 56.

<sup>97</sup> Numerical figures are taken from the Table in Figure 2, exerted from O'Hare and Barrett's article, Regional Inequalities in the Peruvian Tourist Industry.

registered Four Star and ten Five Star hotels in all of Peru, where of the Five Star hotels eight were located in Lima with one each in Trujillo and Cuzco".<sup>98</sup> At this rate, even if tourists do desire to visit other regions of the country, there is little chance of doing so. Tourism will be increasingly difficult to promote if upon arrival, after a treacherous journey on unkept roads, finding decent room and board proves to be just as difficult, with lodging outside of Lima and Cusco being practically obsolete.

The availability of quality hotel accommodations and restaurants is a direct reflection of the amount of investment made into specific departments of Peru. With vigorous promotion it is inevitable that investment will closely follow and vice versa, as they go hand in hand. Consequentially, the correlation between tourist flows and the wealth of regions can be made. This point can be clearly seen through the apparent disparity in the levels of investment *in* and promotion of coastal cities when compared to the rather forsaken Sierra and Selva Departments. Studies have shown that the "higher income, lower poverty coastal Departments" bring in a rather steady inflow of visitors as the infrastructure to support their presence has been made available through the appropriate funding. In contrast, (with the exception of Cuzco, Madre de Dios and Loreto) the Sierra and Selva Departments do not share, on a comparative level, this same kind of success. Proving that "in general most tourists do not visit the poorest regions of the country primarily because the poorer regions in Peru lack tourist resources and/or facilities. A large number of Peru's poorest Departments are then

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<sup>98</sup> O'Hare and Barrett, 56.

subsequently unable to take advantage of any potential benefits which tourism may bring".<sup>99</sup>

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<sup>99</sup> Ibid., 57.

Department	Mean annual number bed nights (foreign) 1985-96	Mean annual number bed nights ×1000/mean pop. (foreign) 1985-96	Mean annual number bednights (domestic) 1985-96	Domestic/foreign bednights ratio 1985-96	Mean number bednights per person (foreign) (domestic) 1985-96	GNP/capita (new soles) 1995	% poverty 1993	Evaluation of tourist attractions (after Mendoza Quintana) 1997
1	2	3	4	5	6	7	8	9
* Sierra Department	344	1.04	67 733	196.9	1.21	2460	51.5	7.96
+ Siva Department	20 717	21.76	416 411	20.1	1.90	2052	29.9	73.74
Amazonas+	588	1.53	123 538	210.1	1.35	1213	47.9	2.76
Ancash	61 178	68.89	520 013	8.5	2.01	8242	18.6	36.6
Apurimac*	1850	3.59	67 895	36.7	2.02	1519	50.8	21.02
Arequipa	4232	3.44	203 982	48.2	2.07	1887	51.7	24.45
Ayacucho*	287 420	282.33	431 130	1.5	2.30	2886	40.6	234.89
Cajamarca*	180	0.46	59 526	330.7	1.32	2593	51.0	10.1
Cuzco*	1554	2.85	365 811	235.4	2.64	1790	47.8	20.24
Huancavelica*	64 104	117.62	525 652	8.2	1.36	4749	15.3	46.58
Huanuco*	4844	4.64	591 936	122.2	1.94	4065	29.4	23.41
Ica	55 662	45.69	784 834	14.1	2.20	5584	22.1	20.28
Junin*	7703	8.66	412 110	53.5	1.69	6273	19.0	12.58
La Libertad	814 677	130.31	3 584 578	4.4	2.70	9776	11.7	64.71
Lambayeque	52 418	76.97	262 090	5.0	1.80	6568	52.8	10.50
Lima/Callao	17 316	288.62	95 238	5.5	2.18	5826	45.4	3.12
Loreto+	2477	20.13	95 612	38.6	1.84	16 992	20.3	7.05
Madre de Dios+	134	0.56	104 560	780.3	1.27	3329	44.6	5.09
Moquegua	12 772	9.49	360 170	28.2	1.75	3704	41.1	12.96
Pasco*	88 670	84.12	186 207	2.1	1.39	1876	33.7	132.46
Piura	2537	4.96	422 917	166.7	1.99	2577	46.8	55.76
Puno*	26 142	128.15	332 917	13.5	1.69	5321	13.9	8.3
San Martin+	9854	67.95	170 318	17.3	1.54	3281	30.8	2.01
Tacna	3395	11.62	210 829	62.1	2.20	3798	43.9	4.64
Tumbes								
Ucayali+								
Average	1.54m	57.64	10.41m	100.54	1.85	4515	35.6	35.05

Source: (a) Foreign and domestic bednights 1985-96, cols 1 and 2, (MITINCI, 1997)  
 (b) Departmental GNP (Instituto Nacional de Estadística e Informática, INEI, 1996)  
 (c) % poverty, col. 8, (UNICEF, 1993)  
 (d) Tourist Attractiveness Index, col. 9, (Mendoza Quintana, 1997)

Figure 2 Number of foreign and domestic bednights ratios; per capita income, percentage living in poverty, and TAI by Department<sup>100</sup>

<sup>100</sup> Figures 2 and 3 based off of study by Mendoza Quintana, exerted from O'Hare and Barrett's article in The Geographic Journal, 1999.



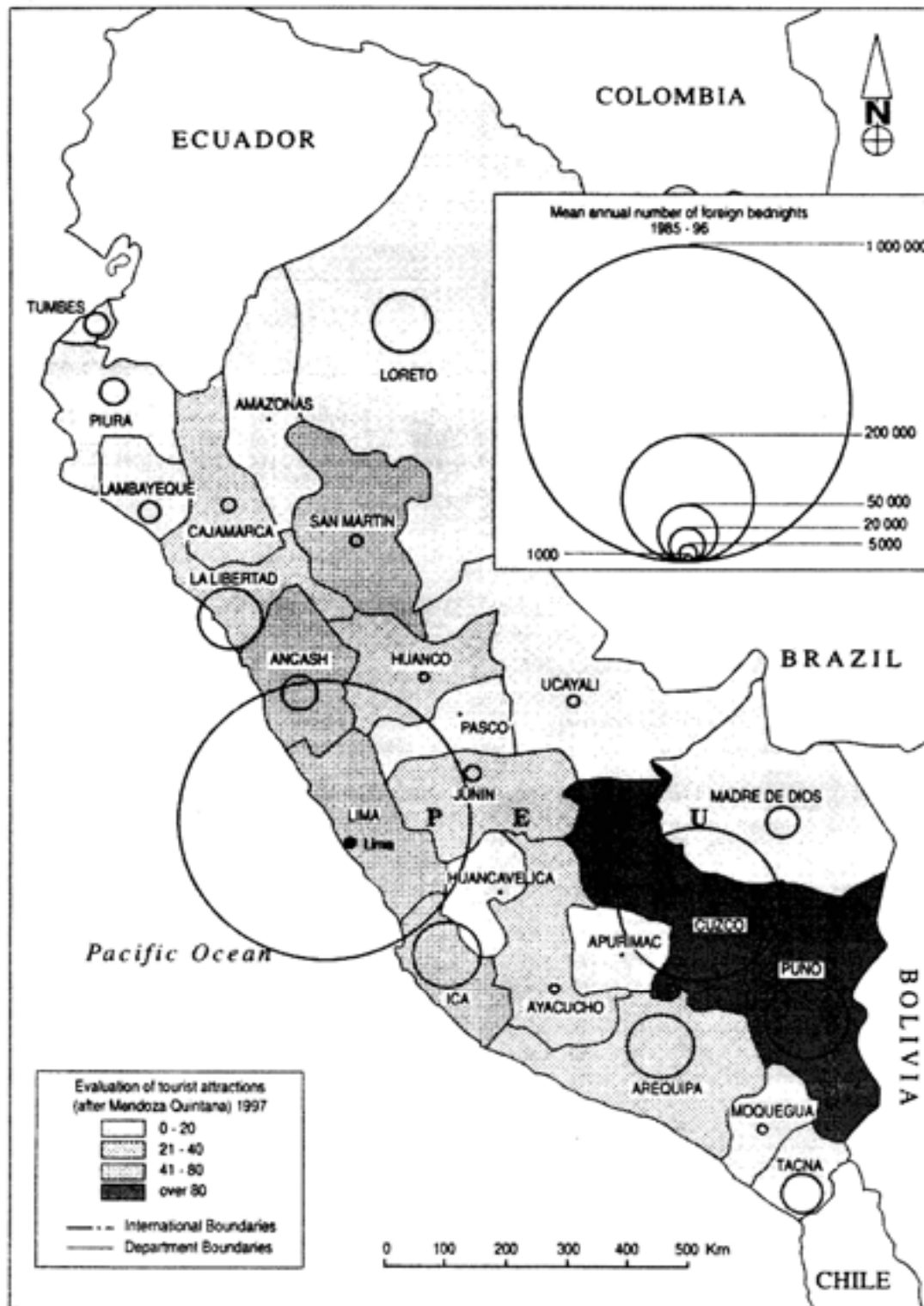


Figure 3 Departmental distribution of the annual (1985-96) bednights in relation to TAI index

**D. CONCLUSION: EFFORTS TO BOLSTER TOURISM- EVOLUTION OF TOURISM IN PERU**

Endorsement of the tourism sector is primarily the responsibility of the Peruvian government, and it is evident through the vast regional inequalities described above, that the administrations that ruled during the periods covered in this essay, failed to develop the tourist industry to its fullest potential. Attempts to bolster tourism however began to surface during the Fujimori government, and despite the regimes corruption-based downfall, efforts have continued to develop through the current administration of Alejandro Toledo (2001-2006).

Foreign investment and the Fujimori administration became synonymous of each other. Contrary to those regimes that preceded him, Fujimori embraced investment wholeheartedly and found it to be the remedy to a majority of Peru's problems. In addition, the government sought to privatize nationalized industries and did so with "two dozen state-run hotels. With the revenue brought in, millions of dollars were spent to improve roads and airports. Tourism projects during this administration totaled more than \$300 million, focusing primarily on hotel construction."<sup>101</sup> The outlook for the industry was encouraging and enrollment in the country's tourism-development institution (CENFOTUR) skyrocketed, broadening the skill base available for employment in the now foreign owned hotels. The economy changed for the better and confidence in Peru began to strengthen accordingly. The capture of Abimael Guzman in September 1992, leader of the Maoist Insurgent group, Sendero Luminoso, added significantly to this newly restored confidence. As a

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<sup>101</sup> Casado, 6.

result, there was an "upward trend in the number of inbound tourists which reached 600,000 in 1996, despite U.S. State Department warnings to its citizens about the dangers of travel in Peru".<sup>102</sup>

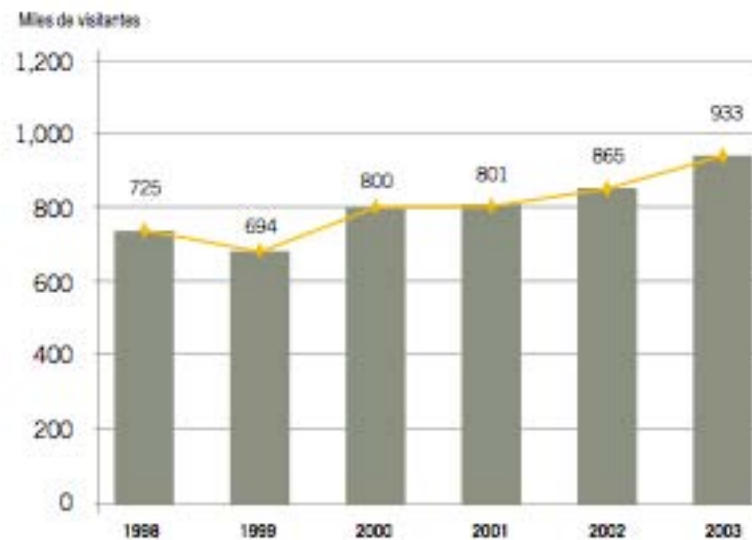
It goes without saying that security is a major concern for all travelers, and while there remain spurts of civil protest in the country, the violence once experienced has been under wraps for nearly a decade. Outside of Peru, security issues have put a damper on the tourism industry, and understandably so. Figure 4<sup>103</sup> demonstrates the gradual rise and evolution of tourist inflow between the years 1998 and 2003. The industry plateaus in 2001, representative of the September 11<sup>th</sup> attacks in New York and Washington D.C. In 2003 however, we see the sector take up again upon the implementation of tighter security measures.

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<sup>102</sup> Casado, 6.

<sup>103</sup> Figure excerpted from PENTUR, PERU: Plan Estratégico de Turismo 2005-2015, Bases Estratégicas developed by MINCETUR Peru, 2005.

### Arribo de visitantes al Perú: 1998-2003



*Fuente: Dirección General de Migraciones y Naturalización - DIGEMIN*  
*Elaboración: MICENTUR*

Figure 4 Numbers of Tourists to Peru 1998-2003

With the demise of the Fujimori regime, Alejandro Toledo took the reigns as president in July of 2001. While his predecessor's administration was tainted with corruption, many of his initial decisions proved to be beneficial to the country and remained in tact. Foreign investment maintained a high level of importance and served to rebuild the country's infrastructure and services. "During the last five years, Peru averaged an economic growth rate of 5 percent or more. Revenue from exports has nearly tripled. Five years ago, 24 percent of Peru's population lived in extreme poverty; today, it's 18 percent. And the unemployment rate is down from 10.5 percent before Toledo took office to 9.1 percent today."<sup>104</sup>

These accomplishments achieved by the Toledo administration reflect constructively on the possibilities

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<sup>104</sup> Ruben Navarrette Jr., "Peru's Toledo Put Country on Right Path" SignOnSanDiego.com (April 23, 2006)

of the development of a more robust tourism industry. To date, a plan has been developed with the goal of promoting the tourism industry and developing it into a primary source of revenue for the country. El Plan Estrategico Nacional de Turismo (PENTUR) has set forth goals for the tourism sector for the years 2005-20015, however as previously mentioned, the overall plan is relatively vague. It identifies strong goals and objectives for the country in terms of tourism development; however an exact process as to how these goals will be achieved is not clearly identified.

In the mean time, improved economic and social conditions have helped rebuild Peru's image, which had previously been severely tainted by violence and corruption. "The importance of image as an influencer of consumer attitude must be taken into consideration by those hoping to promote destinations."<sup>105</sup> While promotion by tourism organizations, such as MITINCI and Promperu for example, facilitate the advertisement of the industry the task of promotion cannot be accomplished by them alone. Image plays a tremendous role in promotion and improvements in this arena come in the form of infrastructural developments. Ultimately, the fate of these developments rest in the hands of policy makers. Implementation of policy focused on the development of a strong infrastructure will cater to the needs of the population and will in turn cater to the need of foreign travelers, thus drawing increased numbers of visitors who seek to broaden their cultural perspectives.

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<sup>105</sup> Lumsdon and Swift, 186.

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## V. CONCLUSIONS

Perhaps the most notable characteristic of the time period covered in this thesis, 1963 to present day, is the lack of change brought to the country via the economic policies implemented. While change is a vague term to use, it encompasses all the areas within the Peruvian infrastructure that are most in need of improvement. As was discussed in Chapter I, the country has stood still in terms of advancement as a majority of the problems identified continue to repeat themselves. Setbacks include, inconsistency of policy, macroeconomic imbalance, economic deficit resulting from excessive external borrowing, an escalating informal sector, and escalating violence. These are most identifiable as they have been the basis of most policies derived by the government. However, it is important to keep in mind that these are all consequences of the underlying and most obvious issues; inequality, poverty, and most importantly under/unemployment. This thesis has proposed the development of tourism as an important mechanism to address these key problems. Tourism is a relatively labor-intensive industry that could provide stable employment in the rural areas of Peru where past development strategies had little or even a negative impact on the quality of life of their inhabitants.

Chapter II examined how various regimes sought to tackle poverty and unemployment, demonstrating that while none of the governments were ignorant of the matters at hand, none were able to implement a plan capable of producing outcomes stable enough to last for longer than a

couple of years. It was not until 1980 that any realistic decision making occurred, reopening the doors to foreign investment, which at the time seemed would be the saving grace for the country. After a number of years without a significant inflow of foreign investment, other than that provided by government borrowing, the country was regressing, both in terms of economic and infrastructure development. Unfortunately, the damage had already been done at the hands of previous regimes and the disillusion in the ruling class led a significant number of Peruvians to join the ranks of the Shining Path. Feeding off of years of failure by the Peruvian government to deliver its promises of increased employment, development of schools to better educate the population so as to alleviate the first issue, and improved living conditions, the Maoist group increased in strength and through their actions, caused for any improvements in the economic condition of the country to be negated. As conditions worsened throughout the first half of the 1980's, the second half was doomed for further failure as the incoming government sought to use the country as an experiment for heterodox policies and other radical ideas such as the nationalization of Peruvian banks. The economy fell to its knees and the lives of the population fell along with it. Unemployment levels soared and the numbers of families living in poverty increased as a consequence of the former. Inflation, a common problem faced by most governments, escalated to levels that could only be managed through a very strict neo-liberal policy that would be implemented by the Fujimori administration in 1990.

Fujimori's government is unique, putting an end to both ISI and democracy as it eventually transformed itself



into an authoritarian regime. Despite the consequential downfall of the administration, as a result of the corruption scandals that kept Fujimori in power nearly three consecutive terms, there is a great deal to learn from this government, both the good and the bad. Most important, is the need to legitimately focus on the issues that are most detrimental to the society and tailor decisions and policy around them in an effort to find a solution. Fujimori's regime demonstrates that hope is not lost for the country in regards to development and bringing itself out of an economic slump. Through foreign investment, tax reforms and privatization, revenue flowed into the country at levels comparable to the 1950's, when the Peruvian economy was at its most stable.

There are tremendous opportunities for Peru in regards to development that combine both growth and employment, and a number of avenues are available to achieve it. Tourism is one of the most promising because Peru has a comparative advantage in providing this service if the attention and funding are appropriately allocated. With an enhanced tourism sector comes a wide array of benefits that serves both the state and its people; enhanced GDP, employment opportunities, opportunities for increased levels of education, infrastructural developments, and environmental protection.

Naturally, with the positive there are always negative aspects that could take shape as a result of the tourist industry; congestion, pollution, commercialization of the culture, etc. However, it is within the purview of the Peruvian state to take adequate steps to mitigate the negative effects.

As demonstrated in Chapter IV, in the section regarding the regional inequalities of the tourism sector, it is obvious that a majority of the counter arguments against tourism derive from the problems that have been seen in Machu Picchu. Keeping in mind that this site is the predominant tourist location in Peru, along with Lima, it draws in a much larger number of tourists than any other region or department in the country, and as a consequence is more apt to experience the negativities that tourism can bring. Interestingly, there are a large number of other departments that share in the folklore that attracts visitors to Machu Picchu and can in fact be appealing to a broader set of interests besides cultural tourism. The problem is that the funding has not been allocated to build up and promote these regions. As we have seen, obtaining the funds to do so is not an issue, provided that money brought into the country through investment, privatization, exports, loans, etc are in fact targeted towards tourism development off of the well-beaten path to Machu Picchu.

It goes without saying that Peru has enormous potential for development, and the development of a more robust tourism sector, while it is a different avenue than most administrations have previously taken, is a strategy that can benefit a majority. Through the efforts made to build an adequate infrastructure to support tourists, the population benefits. Through the investments brought in by the hotel and restaurant sectors, employment is created, educational opportunity enhanced, and poverty reduced. A wider array of promoted attractions disperses the tourist flow more evenly, alleviating the problems of congestion, excess waste, pollution, cultural devaluation, etc. The negative aspects of tourism will always remain a

possibility, however identifying them and increasing awareness of their effects will, if properly monitored and managed, eliminate their potential of occurrence and allow for Peru to flourish and develop to its potential.

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